NO. 77-1550

IN THE

Supreme Court of the United States

October Term, 1978

RECREATIONAL PRODUCTS MARKETING, INC.,
Petitioner

v.

UNITED STATES OF AMERICA,
Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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Petitioner, Recreational Products Marketing, Inc., prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit affirming a judgment of the United States District Court for the Western District of Texas (Waco Division).

OPINIONS BELOW

The Court of Appeals for the Fifth Circuit entered a per curiam affirmance of the District Court's judgment on the basis of the District Court's opinion. The Court of Appeals' affirmance is not reported, having been marked "Do Not Publish," and is reproduced as Appendix A, infra., p. 1a. The District Court's Memorandum

Opinion and Order is not reported officially, is reported unofficially in 76-1 U.S.T.C. par. 16,221, and is reproduced as Appendix B, *infra.*, pp. 2a-9a.

JURISDICTION

The judgment below was entered on February 16, 1978. (Appendix C, *infra.*, pp. 10a-11a.) The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1), this Petition having been timely filed under 28 U.S.C. § 2101(c).

QUESTION PRESENTED

Whether the manufacturer's excise tax upon the first sale of a taxable product may be imposed upon a person, such as the petitioner here, who purchases the product in a completed condition from an unrelated fabricator in an arm's length transaction and who then, without performing any act of manufacture to the product, re-sells the product?

STATUTES INVOLVED

Section 4061(b) of the Internal Revenue Code of 1954 (26 U.S.C.), as applicable to the tax years in question (1970 and 1971) provided:[1]

> Sec. 4061(b). Parts and Accessories—
>
> (1) Except as provided in paragraph (2), there is hereby imposed upon parts or accessories (other than tires and inner tubes) for any of the articles enumerated in subsection (a)(1) sold by the manufacturer, producer, or importer a tax equivalent to 8 percent of the price for which so sold, except that on and after October 1, 1972, the rate shall be 5 percent.

1. Section 4061(b) has been subsequently amended in respects not pertinent to the instant case. Current Code Section 4061(b) is reproduced in Appendix D, *infra.*

Similar Code sections impose a manufacturer's excise tax with respect to other products, so that resolution of the issue in this case under Section 4061(b) will also resolve the issue under those other Code sections. See Sections 4061(a), 4071(a), 4081(a), 4091, 4161 and 4181, which are reproduced in Appendix D, *infra.* Related Code provisions bearing on the issue presented are Sections 4216 and 4219, which are reproduced in Appendix D, *infra.* The pertinent portions of the interpretative Treasury Regulations, Manufacturers and Retailers Excise Tax Regulations §§ 48.0-2 and 48.4216(a)-1 are reproduced in Appendix E, *infra.*

STATEMENT

During the period here pertinent (1970 and 1971), the petitioner engaged in the sale and distribution of auxiliary vehicular gasoline tanks. The petitioner's sole shareholder and chief executive officer, James M. Yates, had designed the tank and was subsequently issued letters patent for the design.

The petitioner engaged the Plastison Division of the Frank Warner Company (hereinafter referred to as "Plastison"), an unrelated party, to fabricate the product according to the petitioner's specifications (including the subsequently patented features). Plastison fabricated products for a number of customers besides the petitioner.

The fabrication process required the use of expensive blow-molding machines, in which Plastison had an investment exceeding $500,000. As is common in the

industry, petitioner agreed to reimburse Plastison for the special molds (costing approximately $10,000), tooling charges and changes, extrusion dies and minor secondary items.

Plastison procured all of the raw materials used in the manufacturing process and performed all of the manufacturing activities. The Government stipulated at trial that the petitioner performed no act of manufacture with respect to the product after it purchased the product from Plastison.

The petitioner purchased all products fabricated by Plastison under the petitioner's design specifications. As is common in such circumstances, Plastison fabricated the product only in response to orders or anticipated orders from petitioner.

Plastison paid federal manufacturer's excise tax on its sales to Petitioner based on a sales price which varied between $7 and $7.50 during the period. The petitioner did not file excise tax returns.

Upon audit, the Commissioner of Internal Revenue determined the petitioner was liable for the manufacturer's excise tax under Section 4061(b) on its sales to its customers. This determination ultimately resulted in the instant suit for refund.

The district court held that the petitioner was the manufacturer of the product and therefore was subject to tax on its sales. The court based its holding on the fact that Plastison sold the products only to petitioner and on the conclusion that "the transfer of tanks to RPM [the petitioner] by Plastison was merely a delivery of previously ordered goods, and not a sale under the excise tax laws". (Appendix B, *infra,* at p. 7a.)

The Court of Appeals affirmed per curiam the District Court's judgment on the basis of the District Court's opinion. (Appendix A, *infra.*)

REASONS FOR GRANTING THE WRIT

1. The decision of the Court of Appeals is in conflict with the decision of the Court of Appeals for the Sixth Circuit in *Air Lift Co. v. United States,* 418 F.2d 558 (1969), affirming on the basis of the district court's opinion, 286 F.Supp. 249 (W.D. Mich. 1968). Prior to the decision in the instant case, the decision in *Air Lift* was the most recent appellate decision addressing the issue presented here. Prior to that decision, however, two other Courts of Appeals had rendered decisions which may be read as consistent with the decision in the instant case and therefore as inconsistent with the decision in *Air Lift.* See *Polaroid Corp. v. United States,* 235 F.2d 276 (C.A. 1, 1956), cert. denied, 352 U.S. 953 (1956); and *Charles Peckat Mfg. Co. v. Jarecki,* 196 F.2d 849 (C.A. 7, 1952), cert. denied, 344 U.S. 875 (1952); but see *Charles Marchand Co. v. Higgins,* 124 F.2d 433 (C.A. 2, 1942).

Although the district court opinion which was adopted by the Court of Appeals in *Air Lift* attempted to distinguish the contrary cases, the distinctions do not appear persuasive. See Judge McCree's dissenting opinion in *Air Lift.* Similarlly, the distinctions raised by the district court in the instant case are not persuasive. The unprincipled and ad hoc application of the statute in these cases and in certain administrative rulings by the Internal Revenue Service has created much confusion in this area and has patently created a situation where taxpayers in different judicial circuits are being taxed differently.

Resolution of the issue raised will resolve the conflict and permit the uniform application of the excise tax throughout the country, which both Congress and the Courts have recognized as particularly important with respect to the manufacturer's excise tax. H. Rep. No. 708, 72 Cong., 1st Sess. 32-33 (1939-1 Cum. Bull. (part 2) 457, 480), accompanying the Revenue Act of 1932, c. 209, 47 Stat. 169; *International Business Machines Corp. v. United States*, 343 F.2d 914, 923 (Ct. Cl. 1965), cert. denied, 382 U.S. 1028 (1966).

2. As will be noted in paragraph 4, *infra*, the decision in the Court below and the decisions in *Polaroid Corp.* and in *Charles Peckat Mfg. Co.* are inconsistent in principle with this Court's decisions in *Indian Motorcycle Co. v. United States*, 283 U.S. 570 (1931) and *F. W. Fitch Co. v. United States*, 323 U.S. 582 (1945).

3. The petitioner believes that the issue presented is of substantial administrative importance. Arrangements whereby taxpayers engage independent parties in arm's length transactions to fabricate products subject to the manufacturer's excise tax are common, and it is not at all unusual for large sums of tax revenue to ride upon the resolution of the issue of which of the parties is the manufacturer subject to tax on its sale of the taxable product. We are unable to make any more precise statement as to potential revenue impact and presume that the Government will advise the Court on that matter.

Equally important to the potential revenue impact from an administration standpoint is the need, evidenced by the conflicting Court of Appeals decisions and the ad hoc application of the statute reflected in various administrative rulings, to establish principles which can guide tax-

payers throughout the country in reporting their tax liabilities and can guide the Internal Revenue Service in the administrative enforcement of the tax. This will permit the certainty of liability contemplated by Congress. H. Rep. No. 708, *supra*, pp. 31 and 32 (1939-1 Cum. Bull. (Part 2), at pp. 479-480).

4. The Court of Appeals' decision here is incorrect. The petitioner was not the manufacturer of the taxable product; stated alternatively, in the approach of this Court in *Indian Motorcycle Co. v. United States*, *supra*, the petitioner did not make the *first* sale of the taxable product.

The petitioner plainly did not perform any of the acts normally understood as manufacturing. A manufacturer, both in the ordinary meaning of the term and in the meaning employed in the manufacturer's excise tax, is the person (Manufacturers and Retailers Excise Tax Regulations, (1954 Code), 48.0-2(a)(4)(i), promulgated by T.D. 7536, and published in 43 Fed. Reg. 13512 (March 31, 1978):[2]

> who produces a taxable article from scrap, salvage or junk material, or from new or raw material by processing, manipulating or changing the form of an article or by combining or assembling two or more articles.

See also, *American Fruit Growers, Inc. v. Brogdex Co.*, 283 U.S. 1 (1931); and *Charles Marchand Co. v. Hig-*

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2. See also the prior Regulations definition contained in Treasury Regulations 46 (1940 ed.), § 316.4, promulgated under the Internal Revenue Code of 1939 and made applicable to 1954 Code by T.D. 6091, 1954-2 Cum. Bull. 47, until superseded by the above Regulation.

Hereinafter all references to the Regulations are to the Manufacturers and Retailers Excise Tax Regulations promulgated by T.D. 7536.

gins, 36 F.Supp. 792, 795 (S.D. N.Y., 1940), aff'd, 124 F.2d 433 (C.A. 2, 1942).

The Government thus correctly conceded that the petitioner did nothing which could constitute any act of manufacture. The Government instead urged a more expansive meaning of the term manufacturer which, because of its unprincipled nature and its ad hoc application to date, is most difficult of statement here with any degree of confidence. The Government seems to be arguing and the Court of Appeals seems to have accepted the legal proposition that a person is a manufacturer when, although he performs no physical acts of manufacture in the common meaning of the term, he owns some patent necessary to the manufacture of the taxable product, engages someone else on an independent contractor basis to perform the acts of manufacture, and acquires the entire taxable product manufactured by that independent contractor. That position was rejected by the court in *Air Lift*. (286 F.Supp. at 253.)

We think it important to distinguish the easy case in which the taxpayer, although not performing the acts of manufacture, is nevertheless treated as the manufacturer because, in essence, his agent performs them for him. Just as a corporate taxpayer may perform manufacturing operations through agents called employees, so a taxpayer may perform them through independent contractors. This occurs when the taxpayer acquires the raw material and, while retaining title thereto at all pertinent times, engages some other party or parties to perform some or even all of the manufacturing processes. E.g., *Acme Juicer Mfg. Co. v. United States*, 202 Ct. Cl. 384 (1973); *Vinal v. Peterson Mortuary, Inc.*, 353 F.2d 814 (C.A. 8, 1965); *Record Guild of America, Inc. v. United States*,

172 F.Supp. 676 (Ct. Cl., 1959); Regulations, § 48.0-2 (a)(4)(ii); see also, *Carbon Steel Co. v. Llewellyn*, 251 U.S. 501 (1920) (involving an excise tax on the net profits of munitions manufacturers).[3] Application of the manufacturer's excise tax in these circumstances is consistent with the normal understanding of the term manufacturer.

These cases, although distinguishable from the instant case, do offer a principled basis for the application of the manufacturer's excise tax. They hold, in essence, that the manufacturer is the person who holds title while the manufacturing process occurs. We think this interpretation is consistent with and indeed compelled by this Court's holding in *Indian Motorcycle Co. v. United States, supra*, that the *first sale* of the taxable product is the taxable event. Obviously, where the taxpayer retains title and merely engages others to perform manufacturing services there will be no sale of a taxable product between them. A sale, both in normal contemplation and in the contemplation of the manufacturer's excise tax connotes a transfer of title. See Treasury Regulations § 48.0-2(a)(5).[4] And, even the Commissioner's own Regula-

3. The Seventh Circuit in *Charles Peckat Mfg. Co.* relied heavily upon *Carbon Steel*, but ignored this Court's emphasis upon title, as well as the special need to read the tax expansively so that all excess war profits from munitions sales were taxed. The latter two factors were not present in *Charles Peckat Mfg. Co.* and are not present here.

4. The Regulations state that a sale involves the transfer of "property (that is, the title or the substantial incidents of ownership)." The substantial incidents of ownership test seems to be addressed to those situations involving the transfer of the substantial burdens and benefits of ownership, although not necessarily bare legal title, such as the situation this Court is currently addressing in *Frank Lyon Company v. United States* (No. 76-624).

tions establish passage of the title as the taxable event. Regulations § 48.0-2(b)(1).

This interpretation is also consistent with this Court's approach to interpretation in analogous contexts. For example, in *Commissioner v. Brown*, 380 U.S. 563 (1965), this Court rejected the Government's attempt to impose an unusual definition of sale into the capital gains provision of the Code and held that, instead, the ordinary definition of that term would apply in the absence of either a congressional indication to the contrary or absurd results.

The petitioner here did not have legal title, within the normal contemplation of the term, at any time during the manufacturing process. And, legal title was transferred to the petitioner only upon the sale from Plastison to petitioner. We do not understand the Government to have urged or either of the Courts below to have held to the contrary. Instead, they have apparently perceived some special meaning of the term in the excise tax laws, and the District Court so indicated in its holding that the transaction "was not a sale under the excise tax laws." However, as was the case in *Commissioner v. Brown*, *supra*, there is no justification for departing from common understanding of the term *sale*, particularly since to do so will inject confusion and ad hoc application of the tax contrary to Congress' express intent that there be certainty of liability. See H. Rep. No. 708, *supra*, pp. 31 and 32.

The district court below, as did the courts in *Polaroid Corp.* and *Charles Peckat Mfg. Co.*, seems to have been persuaded by the conclusion that the patent holder (here, the petitioner) had some form of "proprietary"

interest in the product as it was manufactured. The Government also advanced this concept in its brief on appeal. Neither the courts nor the Government explained precisely what a "proprietary" interest is or how it relates to the congressional purpose to apply the tax to a sale—i.e., a transfer of title for consideration. Apparently, the notion is that, because the patent holder can require the fabricator to sell only to him, somehow magically the patent holder must be the manufacturer. Yet the same consideration applies equally to products manufactured with a protected trademark or brand name, and the courts and the Government have long recognized that that alone will not suffice to render a trademark or brand name owner the manufacturer. See *Charles Marchand Co. v. Higgins*, 124 F.2d 433 (C.A. 2, 1942); Rev. Rul. 60-42, 1960-1 Cum. Bull. 474; and Rev. Rul. 58-114, 1958-1 Cum. Bull. 424.

The Government may urge that the trademark or brand name example is distinguished from the patent situation because the fabricator is free to produce products of the same design for sale to others. Putting aside the fact that the agreement with the trademark or brand name owner may prevent such sales, that is hardly a basis for distinction. The Government's long-standing position is that, just as a patented product is unique for purposes of the excise tax laws, so a trademark or brand name product is unique. E.g., see Rev. Rul. 63-238, 1963-2 Cum. Bull. 519; Rev. Rul. 70-44, 1970-1 Cum. Bull. 228.[5] In both

5. These rulings interpret the constructive sales price provisions of Section 4216(b). Basically, those provisions apply the excise tax to a tax base *other* than the actual price for which the manufacturer sells the taxable product in certain circumstances. For example, under Section 4216(b)(1)(C), when a manufacturing corporation sells the taxable product to a related sales corporation

instances, the economic value inheres in the ultimate consumer's real or perceived belief that he is purchasing a product which, because of its uniqueness, will serve his purposes better than other products.

Indeed, in the final analysis, the attempt to treat the patent owner as the manufacturer making the first sale seems to be based upon misguided attempts to breathe equity into the excise tax laws. In *Polaroid Corp.* the principal concern of the court was that because, in many instances, a fabricator will pay an unrelated patent holder a license fee which must be built into his sales price for the product, he will pay a higher tax than will someone who does not pay a license fee. (The Government advanced this notion in its appellate brief in the instant case.) This, of course, may be viewed as creating some form of competitive distortion, but this Court has

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which, in turn, sells to unrelated wholesale distributors, the Internal Revenue Service has successfully taken the position that the tax base is the selling corporation's sales price to unrelated wholesale distributors rather than the manufacturing corporation's sales price. See Rev. Rul. 62-68, 1962-1 Cum. Bull. 216; and *Creme Mfg. Co. v. United States*, 492 F.2d 515 (C.A. 5, 1974). Importantly, even when (as in *Creme Mfg. Co.*, and in *Columbia Products Co. v. United States*, 404 F.Supp. 276 (D. S.C., 1975), opinion withdrawn by order), the selling corporation owned the trademark or brand name and had effective control over the manufacturing corporation, the Government has not urged that the selling corporation was the manufacturer making the first sale of the product. We think rightly so, for there has clearly been a sale by the manufacturing corporation to the selling corporation and a special Code Section must be used to apply the tax to any base other than that sales price. Section 4216, as Section 4219 (applying an analogous special rule for certain transfers of title), thus evidences Congress' unmistakable intention to tax the amount paid upon the first transfer of legal title and to suspend that rule only in those circumstances expressly provided. Because of the complexity of the constructive sales price provisions, however, extended briefing is necessary to fully address their implications to the instant case.

clearly indicated that that is *not* a factor to be considered in determining the tax base (i.e., sales price) to which the tax is applied.

In *F. W. Fitch Co. v. United States, supra,* this Court refused to exclude from the tax base certain costs, such as advertising and selling expenses which, the taxpayer there urged, are not normally costs of manufacture and hence not within the spirit of the tax on the *manufacturer's* sales price. The Court refused to adopt unique definitions simply because a manufacturer who incurs advertising and selling costs will be discriminated against vis-a-vis a manufacturer who does not (such as private brand manufacturers where the customer incurs the costs). This Court held that that was simply an inequity flowing inevitably from the application of the tax to the manufacturer's sales price. So too, in the instant case, the application of the tax to the first sale involving a transfer of title after manufacturing is completed is commanded by the statute and the courts should not, as the Court did in *Polaroid Corp.*, sit as courts of equity on an ad hoc basis to correct inequities, real or perceived.

Finally, the courts below, as did the courts in *Polaroid Corp.* and *Charles Peckat Mfg. Co.*, erred in relying upon the petitioner's purchase of the special molds and payment of special charges. As the Commissioner's own recently promulgated Regulations establish, this is a factor to consider in adjusting the sales price from Plastison to the petitioner rather than a factor to be considered in ignoring that sale. Regulations § 48.4216(a)-1(a) requires that the taxable sales price include "the total consideration paid for an article whether that consideration is in the form of money, services or other things," so that

collateral costs such as special charges separately stated from the sales price are to be added to the stated sales price in reaching a proper tax base. Special tools and dies supplied by a purchaser are covered specifically. Section 48.4216(a)-1(b). These special adjustments insure that these costs are appropriately reflected in the tax base upon the critical event—the *first* sale of the product. Logically, these factors are worthy of no further consideration in ignoring that sale. Yet, the courts did consider them and relied prominently upon them in reaching their decisions.[6]

In summary, the tax is properly imposed upon the sale occurring at the time title to the manufactured product is transferred for consideration. Here, Plastison transferred title to the petitioner and became subject to the tax. The petitioner, having performed no manufacturing activity after acquiring title by purchase, is not subject to the tax.

6. The Regulations state an effective date after May 5, 1974, for the tools and dies adjustment. The effective date appears to be an exercise of discretion under Code § 7805(b). In Rev. Rul. 74-201, 1974-1 Cum. Bull. 314, the Government adopted this position and overruled a prior contrary position. The effective date of the ruling is May 6, 1974. Assuming the validity of the Regulation (which we would seriously doubt the Government will deny), it must logically follow that, just as this factor is not a consideration in determining who is the manufacturer making the first sale in periods after the effective date, so it is not a consideration in making that inquiry in periods prior to the effective date since no change in the statute was involved.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

DO NOT
PUBLISH

In The
UNITED STATES COURT OF APPEALS
For The Fifth Circuit

No. 76-2575

RECREATIONAL PRODUCTS MARKETING, INC.,
Plaintiff-Appellant,

v.

UNITED STATES OF AMERICA,
Defendant-Appellee.

Appeal from the United States District Court
for the Western District of Texas

(February 16, 1978)

Before THORNBERRY, AINSWORTH and MORGAN, Circuit Judges.

PER CURIAM:

Affirmed on the basis of the opinion of District Judge Jack Roberts dated April 9, 1976.

AFFIRMED.

APPENDIX B

In The

UNITED STATES DISTRICT COURT

Western District of Texas

Waco Division

C.A. NO. W-74-CA-77

RECREATIONAL PRODUCTS MARKETING, INC.,

v.

UNITED STATES OF AMERICA

MEMORANDUM OPINION AND ORDER

This is a suit in which Plaintiff, Recreational Products Marketing, Inc. [hereinafter referred to as RPM], seeks to recover $26,686.15 in manufacturer's excise taxes, plus statutory interest. The case was tried before the Court on March 15, 1976, and after carefully considering the evidence, the Court enters this Memorandum Opinion and Order which shall constitute findings of fact and conclusions of law.

Plaintiff, pursuant to 28 U.S.C. §§ 1340 and 1346, seeks recovery of $26,686.15 in manufacturer's excise taxes imposed upon it for the periods of June 30, 1970 through December 31, 1971. RPM is a Waco, Texas corporation which distributes automobile parts and accessories. For the relevant time periods it was engaged chiefly in the sale and distribution of plastic auxiliary vehicular tanks which were to be used primarily on

pickups for storing extra fuel or water. The plastic tanks were fabricated by Plastison, Division of Frank Warner Corporation, a now bankrupt Minnesota corporation, and the tanks were then delivered to RPM to be sold to its customers.

There are two issues in this case. First, whether RPM was the manufacturer of the tanks for federal excise tax purposes, and second, if RPM was the manufacturer, upon what sales price should the excise tax be based. The relevant statute provides in part that "there is hereby imposed upon parts and accessories . . . for any [automobile or truck] sold by the manufacturer . . . a tax equivalent to 8 percent of the price for which so sold. . .". 26 U.S.C. § 4061(b)(1).

After an audit by the Internal Revenue Service, the Government declared that RPM was the manufacturer of the tanks under this statute, although Plastison had previously paid the excise taxes on the tanks. The manufacturer's excise tax is imposed only on the first sale of a product which is subject to the tax. *Indian Motorcycle Company v. United States*, 283 U.S. 570 (1931). Thus, if Plastison's delivery of the tanks to RPM was a sale and it was the statutory manufacturer, the tax it paid was proper. If RPM was the statutory manufacturer, however, it should have paid the tax based on its sale of the tanks to its customers. It is undisputed that the sale of the tanks was taxable under 26 U.S.C. 4061(b)(1).

RPM relies heavily on *Air Lift Company v. United States*, 286 F.Supp. 249 (W. D. Mich. 1968), *aff'd*, 418 F.2d 558 (6th Cir. 1969), where the Court held that the fabricators of inflatable rubber cylinders were the manufacturers for purposes of the excise tax. RPM claims that

it should not be the manufacturer based on the reasoning used by the Court in *Air Lift*. The Court held that Air Lift Company, which bought the inflatable booster devices from large rubber companies, was not the manufacturer because of several prominent factors. The fabricators completely controlled the actual process of making the rubber cylinders. The expensive machinery necessary to produce the cylinders was owned by the fabricators, and the labor and all material required to produce the cylinders were provided by the fabricator. Thus, the fabricator took all the risks of production. The Court further found that the agreements between Air Lift Company and the large rubber companies were arms-length transactions and that the fabricators assumed they were manufacturers under the excise tax laws and therefore paid the taxes. The Court also found that the fabricators could sell the cylinders to other companies as long as they were not sold as spring suspension devices, since Air Lift owned the patent for the use of the cylinder as such a device.

RPM contends that it is in the same position as Air Lift, and in many ways it is. Plastison, the fabricator, owns the more expensive equipment used to produce the polyethylene tanks by a process called blow molding. Plastison was responsible for obtaining all labor and materials for the production of the tanks, and according to the testimony at trial the agreement by Plastison to produce the tanks for RPM was an arms-length agreement between the representatives of the two companies. Nevertheless, the Court finds that there are significant facts which distinguish RPM from the Air Lift Company and therefore require that RPM be found the manufacturer for excise tax purposes.

By finding RPM the manufacturer, the Court necessarily agrees with the Government that the case at bar is more analogous to *Charles Peckat Mfg. Co. v. Jarecki*, 196 F.2d 849 (7th Cir. 1952), *cert. denied*, 344 U.S. 875 (1952) and *Polaroid Corporation v. United States*, 235 F.2d 276 (1st Cir. 1956), *cert. denied*, 352 U.S. 953 (1956) and other cases relied on by the Government. In *Peckat* the Court held that Peckat, the taxpayer who ordered sun visors from a fabricator, was the manufacturer primarily for the following reasons: 1) the ownership of the patent of an essential part of the visor was with Peckat, 2) the contract between the parties indicated that the fabricator would produce the visors only upon Peckat's request, 3) the fabricator could not sell visors to other buyers if Peckat's patent had been used in their production, 4) the disposition of the visors was directed by Peckat, 5) the fabricator had no proprietary interest in the completed product, and 6) Peckat owned the tools and dies necessary to produce the visors.

In holding that the Polaroid Corporation was the manufacturer of a camera under the excise tax laws the Court emphasized the following facts: 1) Polaroid owned the patent for the cameras, 2) Polaroid controlled the output of cameras, 3) Polaroid realized the loss or gain because of any increased or decreased costs of production, and 4) the specialized tools for making the camera were owned by Polaroid. *Polaroid Corporation v. United States, supra.*

The case at bar can be distinguished in slight ways from cases relied on by both RPM and by the Government, and it appears to the Court to be a closer case than any of the previously discussed cases. It was the burden of RPM to show that it was not the manufacturer, how-

ever, *see Charles Peckat Mfg. Co. v. Jarecki, supra,* and the Court concludes that RPM has not sustained its burden.

RPM during the time in question was wholly owned and operated by James M. Yates, who in 1970 had applied for the design patent on the auxiliary vehicular tanks in question. The patent was granted to Yates in 1972. RPM reimbursed Plastison for the expensive [approximately $10,000] molds which were essential to produce the tanks. RPM also paid for tooling charges and changes, extrusion dies, and what has been referred to as minor secondary items, all of which were necessary for the production of the auxiliary tanks. RPM therefore owned the specialized equipment necessary to produce its tanks and in fact the evidence indicated RPM was aware of this by the fact that it had insured and depreciated the molds while they were in Plastison's possession. Although RPM emphasized at trial that it had no obligation to buy any of the tanks produced by Plastison, the Court finds that Plastison did not make the tanks unless it had an order from RPM or anticipated an order. The tanks would not have been produced without a request by RPM. Additionally every tank fabricated by Plastison using RPM's design, molds, and other tools was delivered to RPM. The evidence did not indicate that an express agreement existed preventing Plastison from selling the tanks on its own, but it is clear from all the evidence that the disposition of the tanks in question was controlled by RPM. This is the primary distinction between this case and *Air Lift Company v. United States, supra.*

It further appears that no real proprietary interest in the products as auxiliary fuel or water tanks existed at

the time they were produced by Plastison. The plastic tanks alone were totally useless. It was only after RPM had paid for their delivery and had added metal straps, hoses, valves, and nuts and bolts that it became possible for the tanks to be used for the purpose for which they were intended—auxiliary vehicular tanks for pickups. The Court therefore concludes that the transfer of the tanks to RPM by Plastison was merely a delivery of previously ordered goods, and not a sale under the excise tax laws. This leads to the conclusion that RPM was the manufacturer of the tanks during the period in question and was liable for the excise taxes pursuant to 26 U.S.C. § 4061(b)(1).

Since RPM was the manufacturer, its federal excise tax liability ordinarily should be computed on the basis of the actual price it charged its distributors for the tanks. *See Creme Manufacturing Co., Inc. v. United States,* 492 F.2d 515 (5th Cir. 1974). RPM claims that it falls within an exception to this rule, which provides:

> If an article is sold at retail or to a retailer, and if . . .
>
> (A) the manufacturer . . . sells such articles at retail, or to retailers . . .,
>
> (B) the manufacturer . . . of such articles regularly sells such articles to one or more wholesale distributors in arm's length transactions and he establishes that his prices in such cases are determined without regard to any tax benefit under this paragraph,
>
> (C) in the case of articles upon which tax is imposed under section 4061(a) . . ., and

> (D) the transaction is an arm's length transaction
>
> the tax . . . shall . . . be computed on whichever of the following prices is lower: (i) the price for which such article is sold, or (ii) the highest price for which such articles are sold by such manufacturer . . . to wholesale distributors (other than special dealers).

26 U.S.C. § 4216(b)(2).

This statute as applied to this case simply means that if RPM sold the tanks to both retailers and wholesalers, its excise tax should have been based on the highest price paid for the tanks by its wholesalers. The Government has assessed the tax based on a price of $63.60 per two tank unit. Yates, RPM's owner, testified that it sold the tanks in pairs to wholesalers for a high price of $54.50 and that it did not make retail sales to these wholesalers although some of its wholesalers made retail sales. The Government did not dispute this contention at trial, nor did it have evidence to the contrary. The Court therefore finds that the excise tax paid by RPM for the period in question should have been based on its highest price to its wholesalers, which was $54.50. It is accordingly

ORDERED, ADJUDGED, and DECREED that the Government properly held that Plaintiff was the manufacturer of the auxiliary vehicular tanks during the periods in question, under 26 U.S.C. § 4061(b)(1); that the price upon which Plaintiff's excise tax should have been based during these periods was $54.50 for each pair of tanks sold, pursuant to 26 U.S.C. § 4216(b)(2); and that the relief requested by Plaintiff in all other respects be, and hereby is, DENIED.

Entered this 9th day of April, 1976, at Austin, Texas.

/s/ JACK ROBERTS
Jack Roberts
United States District Judge

APPENDIX C

UNITED STATES COURT OF APPEALS
For The Fifth Circuit

No. 76-2575

D. C. Docket No. W-74-CA-77

RECREATIONAL PRODUCTS MARKETING, INC.,
Plaintiff-Appellant,

v.

UNITED STATES OF AMERICA,
Defendant-Appellee.

Appeal from the United States District Court for the Western District of Texas

Before THORNBERRY, AINSWORTH and MORGAN, Circuit Judges.

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Western District of Texas, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of

the said District Court in this cause be, and the same is hereby, affirmed;

It is further ordered that plaintiff-appellant pay to defendant-appellee, the costs on appeal to be taxed by the Clerk of this Court.

February 16, 1978

ISSUED AS MANDATE: March 10, 1978

APPENDIX D

INTERNAL REVENUE CODE OF 1954

(26 U.S.C.)

Sec. 4061(a) Trucks, Buses, Tractors, Etc.—

(1) Tax Imposed.—There is hereby imposed upon the following articles (including in each case parts or accessories therefor sold on or in connection therewith or with the sale thereof) sold by the manufacturer, producer, or importer a tax of 10 percent of the price for which so sold, except that on and after October 1, 1979, the rate shall be 5 percent—

Automobile truck chassis.
Automobile truck bodies.
Automobile bus chassis.
Automobile bus bodies.
Truck and bus trailer and semitrailer chassis.
Truck and bus trailer and semitrailer bodies.
Tractors of the kind chiefly used for highway transportation in combination with a trailer or semitrailer.

A sale of an automobile truck, bus, truck or bus trailer or semitrailer shall, for the purposes of this subsection, be considered to be a sale of a chassis and of a body enumerated in this subsection.

(2) Exclusion for Light-Duty Trucks, Etc.—The tax imposed by paragraph (1) shall not apply to a sale by the manufacturer, producer, or importer of the following articles suitable for use with a vehicle having a gross

vehicle weight of 10,000 pounds or less (as determined under regulations prescribed by the Secretary or his delegate)—

Automobile truck chassis.
Automobile truck bodies.
Automobile bus chassis.
Automobile bus bodies.

Truck trailer and semitrailer chassis and bodies, suitable for use with a trailer or semitrailer having a gross vehicle weight of 10,000 pounds or less (as so determined).

(b) Parts and accessories.—

(1) Except as provided in paragraph (2), there is hereby imposed upon parts or accessories (other than tires and inner tubes) for any of the articles enumerated in subsection (a)(1) sold by the manufacturer, producer, or importer a tax equivalent to 8 percent of the price for which so sold, except that on and after October 1, 1979, the rate shall be 5 percent.

(2) No tax shall be imposed under this subsection upon any part or accessory which is suitable for use (and ordinarily is used) on or in connection with, or as a component part of, any chassis or body for a passenger automobile, any chassis or body for a trailer or semi-trailer suitable for use in connection with a passenger automobile, or a house trailer.

* * *

§ 4071. Imposition of tax

(a) Imposition and rate of tax.—There is hereby imposed upon the following articles, if wholly or in part of rubber, sold by the manufacturer, producer, or importer, a tax at the following rates:

(1) Tires of the type used on highway vehicles, 10 cents a pound.

(2) Other tires (other than laminated tires to which paragraph (5) applies), 5 cents a pound.

(3) Inner tubes for tires, 10 cents a pound.

(4) Tread rubber, 5 cents a pound.

(5) Laminated tires (not of the type used on highway vehicles) which consist wholly of scrap rubber from used tire casings with an internal metal fastening agent, 1 cent a pound.

* * *

§ 4081. Imposition of tax

(a) In general.—There is hereby imposed on gasoline sold by the producer or importer thereof, or by any producer of gasoline, a tax of 4 cents a gallon.

* * *

§ 4091. Imposition of tax

There is hereby imposed on lubricating oil (other than cutting oils) which is sold in the United States by the manufacturer or producer a tax of 6 cents a gallon, to be paid by the manufacturer or producer.

* * *

§ 4161. Imposition of tax

(a) Rods, creels, etc.—There is hereby imposed upon the sale of fishing rods, creels, reels, and artificial lures, baits, and flies (including parts or accessories of such articles sold on or in connection therewith, or with the sale thereof) by the manufacturer, producer, or importer a tax equivalent to 10 percent of the price for which so sold.

(b) Bows and arrows, etc.—

(1) Bows and arrows.—There is hereby imposed upon the sale by the manufacturer, producer, or importer—

(A) of any bow which has a draw weight of 10 pounds or more, and

(B) of any arrow which measures 18 inches overall or more in length,

a tax equivalent to 11 percent of the price for which so sold.

(2) Parts and accessories.—There is hereby imposed upon the sale by the manufacturer, producer, or importer —

(A) of any part or accessory (other than a fishing reel) suitable for inclusion in or attachment to a bow or arrow described in paragraph (1), and

(B) of any quiver suitable for use with arrows described in paragraph (1),

a tax equivalent to 11 percent of the price for which so sold.

* * *

§ 4181. Imposition of tax

There is hereby imposed upon the sale by the manufacturer, producer, or importer of the following articles a tax equivalent to the specified percent of the price for which so sold:

Articles taxable at 10 percent—

Pistols.
Revolvers.

Articles taxable at 11 percent—

Firearms (other than pistols and revolvers)
Shells, and cartridges.

* * *

§ 4216. Definition of price

(a) Containers, Packing and Transportation Charges. —In determining, for the purposes of this chapter, the price for which an article is sold, there shall be included any charge for coverings and containers of whatever nature, and any charge incident to placing the article in condition packed ready for shipment, but there shall be excluded the amount of tax imposed by this chapter, whether or not stated as a separate charge. A transportation, delivery, insurance, installation, or other charge (not required by the foregoing sentence to be included) shall be excluded from the price only if the amount thereof is established to the satisfaction of the Secretary in accordance with the regulations.

(b) Constructive sale price—

(1) In general.—If an article is—

(A) sold at retail,
(B) sold on consignment, or
(C) sold (otherwise than through an arm's length transaction) at less than the fair market price,

the tax under this chapter shall (if based on the price for which the article is sold) be computed on the price for which such articles are sold, in the ordinary course of trade, by manufacturers or producers thereof, as determined by the Secretary or his delegate. In the case of an article sold at retail, the computation under the preceding sentence shall be on whichever of the following prices is the lower: (i) the price for which such article is sold, or (ii) the highest price for which such articles are sold to wholesale distributors, in the ordinary course of trade, by manufacturers or producers thereof, as determined by the Secretary or his delegate. This paragraph shall not apply if paragraph (2) applies.

(2) Special rule.—If an article is sold at retail or to a retailer, and if—

(A) the manufacturer, producer, or importer of such article regularly sells such articles at retail, or to retailers, as the case may be,

(B) the manufacturer, producer, or importer of such article regularly sells such articles to one or more wholesale distributors in arm's length transactions and he establishes that his prices in such cases are determined without regard to any tax benefit under this paragraph,

(C) in the case of articles upon which tax is imposed under section 4061(a) (relating to trucks,

buses, tractors, etc.), the normal method of sales for such articles within the industry is not to sell such articles at retail or to retailers, or combinations thereof, and

(D) the transaction is an arm's length transaction,

the tax under this chapter shall (if based on the price for which the article is sold) be computed on whichever of the following prices is the lower: (i) the price for which such article is sold, or (ii) the highest price for which such articles are sold by such manufacturer, producer, or importer to wholesale distributors (other than special dealers).

(3) Constructive sale price in case of certain articles.—Except as provided in paragraphs (4) and (5), for purposes of paragraph (1), if—

(A) the manufacturer, producer, or importer of an article regularly sells such article to a distributor which is a member of the same affiliated group of corporations (as defined in section 1504(a)) as the manufacturer, producer, or importer, and

(B) such distributor regularly sells such article to one or more independent retailers, but does not regularly sell to wholesale distributors,

the constructive sale price of such article shall be 90 percent of the lowest price for which such distributor regularly sells such article in arm's-length transactions to such independent retailers. The price determined under this paragraph shall not be adjusted for any exclusion (except for the tax imposed on such article) or readjustments

under subsections (a) and (e) and under section 6416 (b)(1). If both this paragraph and paragraph (4) apply with respect to an article, the constructive sale price for such article shall be the lower of the constructive sale price determined under this paragraph or paragraph (4).

(4) Constructive sale price in case of certain other articles.—For purposes of paragraph (1), if—

(A) the manufacturer, producer, or importer of an article regularly sells (except for tax-free sales) only to a distributor which is a member of the same affiliated group of corporations (as defined in section 1504(a)) as the manufacturer, producer, or importer,

(B) the distributor regularly sells (except for tax-free sales) such article only to retailers, and

(C) the normal method of sales for such articles within the industry by manufacturers, producers, or importers is to sell such articles in arm's-length transactions to distributors,

the constructive sale price for such article shall be the price at which such article is sold to retailers by the distributor, reduced by a percentage of such price equal to the percentage which (i) the difference between the price for which comparable articles are sold to wholesale distributors, in the ordinary course of trade, by manufacturers or producers thereof, and the price at which such wholesale distributors in arm's-length transactions sell such comparable articles to retailers, is of (ii) the price at which such wholesale distributors in arm's-length transactions sell such comparable articles to retailers. The price determined under this paragraph shall not be adjusted for any exclusion (except for the tax imposed on

such article) or readjustment under subsections (a) and (e) and under section 6416(b)(1).

(5) Constructive sale price in the case of automobiles, trucks, etc.—In the case of articles the sale of which is taxable under section 4061(a) (relating to trucks, buses, tractors, etc.), for purposes of paragraph (1), if—

(A) the manufacturer, producer, or importer of the article regularly sells such article to a distributor which is a member of the same affiliated group of corporations (as defined in section 1504(a)) as the manufacturer, producer, or importer, and

(B) such distributor regularly sells such article to one or more independent retailers,

the constructive sale price of such article shall be 98½ percent of the lowest price for which such distributor regularly sells such article in arm's-length transactions to such independent retailers. The price determined under this paragraph shall not be adjusted for any exclusion (except for the tax imposed on such article) or readjustments under subsections (a) and (e) and under section 6416(b)(1).

(6) Definition of lowest price.—For purposes of paragraphs (1), (3), and (5), the lowest price shall be determined—

(A) without requiring that any given percentage of sales be made at that price, and

(B) without including any fixed amount to which the purchaser has a right as a result of contractual arrangements existing at the time of the sale.

* * *

§ 4219. Application of tax in case of sales by other than manufacturer or importer

In case any person acquires from the manufacturer, producer, or importer of an article, by operation of law or as a result of any transaction not taxable under this chapter, the right to sell such article, the sale of such article by such person shall be taxable under this chapter as if made by the manufacturer, producer, or importer, and such person shall be liable for the tax.

APPENDIX E

Manufacturer's and Retailers Excise Tax Regulations (26 C.F.R.) (1954 Code).

§ 48.0-2 General definitions and attachment of tax.

(a) *Meaning of terms.* As used in the regulations in this part, unless otherwise expressly indicated—

* * *

(4) (i) The term "manufacturer" includes any person who produces a taxable article from scrap, salvage, or junk material, or from new or raw material, by processing, manipulating, or changing the form of an article or by combining or assembling two or more articles. The term also includes a "producer" and an "importer". An "importer" of a taxable article is any person who brings such an article into the United States from a source outside the United States, or who withdraws such an article from a customs bonded warehouse for sale or use in the United States. If the nominal importer of a taxable article is not its beneficial owner (for example, the nominal importer is a customs broker engaged by the beneficial owner), the beneficial owner is the "importer" of the article for purposes of chapter 32 and is liable for tax on his sale or use of the article in the United States. See section 4219 and the regulations thereunder for the circumstances under which sales by persons other than the manufacturer or importer are subject to the manufacturers excise tax.

(ii) Under certain circumstances, as where a person manufactures or produces a taxable article for another person who furnishes materials under an agreement

whereby the person who furnished the materials retains title thereto and to the finished article, the person for whom the taxable article is manufactured or produced, and not the person who actually manufactures or produces it, will be considered the manufacturer.

(iii) A manufacturer who sells a taxable article in a knockdown condition is liable for the tax as a manufacturer. Whether the person who buys such component parts and assembles a taxable article from them will also be liable for tax as a further manufacturer of a taxable article will depend on the relative amount of labor, material, and overhead required to assemble the completed article and on whether the article is assembled for a business or personal use. See section 4218 and the regulations thereunder.

(5) The term "sale" means an agreement whereby the seller transfers the property (that is, the title or the substantial incidents of ownership) in goods to the buyer for a consideration called the price, which may consist of money, services, or other things.

* * *

(b) *Attachment of tax.* (1) For purposes of this part, the manufacturers excise tax generally attaches when the title to the article sold passes from the manufacturer to a purchaser, and the retailers excise tax generally attaches when the title to the article sold passes from the retailer to a purchaser.

(2) When title passes is dependent upon the intention of the parties as gathered from the contract of sale and the attendant circumstances. In the absence of expressed intention, the legal rules of presumption followed in the

jurisdiction where the sale is made govern in determining when title passes.

* * *

§ 48.4216(a)-1. Charges to be included in sale price.—(a) *In general.* The "price" for which an article is sold includes the total consideration paid for the article, whether that consideration is in the form of money, services, or other things. See § 48.0-2(a)(5). However, for purposes of the taxes imposed under chapter 32 certain collateral charges made in connection with the sale of a taxable article must be included in the taxable sale price, whereas others may be excluded. Any charge which is required by a manufacturer, producer, or importer to be paid as a condition of its sale of a taxable article and which is not attributable to an expense falling within one of the exclusions provided in section 4216 or the regulations thereunder is includible in the taxable sale price. It is immaterial for this purpose that the charge may be paid to a person other than the manufacturer, producer, or importer, or that it may be separately billed to the purchaser as a charge earmarked for expenses incurred or to be incurred in his behalf, such as charges for demonstration or display of the article, for sales promotion programs, or otherwise. With respect to the rules relating to exclusion (in the case of sales after December 31, 1960) of charges for local advertising of a manufacturer's products, see section 4216(e) and § 48.4216(e)-1. In the case of sales on credit, a carrying, finance, or service charge is excludable from the sale price if it is reasonably related to the costs of carrying the deferred portion of the sale price (such as interest on the deferred portion of the sale price, expenses of bookkeeping neces-

sary to keep the records of such sales, and expenses of correspondence and other communication in connection with collection).

(b) *Tools and dies.* Separate charges for tools and dies used in the manufacture or production of a taxable article are to be included, in whole or in part, in the sale price on which the tax is based. It is immaterial whether the charges for such items are billed in a lump sum or are amortized or allocated to each of the taxable articles. If, at the termination of a contract to manufacture taxable articles, the tools and dies used in production pass to the purchaser, only the amount of depreciation of the tools and dies incurred in production, computed on a "production output" basis, should be included in the sale price. If the purchaser furnishes the tools and dies, the amount of the cost thereof, to the extent that such cost has been depreciated in the production of the taxable articles (computed on a "production output" basis), shall be included in determining the sale price of the articles for purposes of computing the tax. This paragraph applies to sales by manufacturers after May 5, 1974.

No. 77-1550

In the Supreme Court of the United States

OCTOBER TERM, 1977

RECREATIONAL PRODUCTS MARKETING, INC.,
PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

WADE H. MCCREE, JR.,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1550

RECREATIONAL PRODUCTS MARKETING, INC.,
PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

The question presented in this federal excise tax case is whether petitioner was the "manufacturer" of certain gasoline tanks within the meaning of Section 4061(b) of the Internal Revenue Code of 1954 (26 U.S.C.), so as to make its sales of those tanks subject to excise tax.

The pertinent facts are as follows: Petitioner is a corporation wholly owned by James M. Yates, who created an original design for an auxiliary vehicular gasoline tank. In 1970, Yates applied for a patent covering the tanks and was issued a design patent on February 29, 1972. In 1970, petitioner entered into an agreement with Plastison, Inc., under which that company was to manufacture the tanks, using Yates' design, at a cost to petitioner of approximately $7.50 per tank. The tanks

were to be produced by a process known as "blow-molding," using machines owned by Plastison. Production of the tanks by this process required the use of specialized molds costing approximately $10,000. As part of its agreement, petitioner reimbursed Plastison for the cost of those molds, and also paid for tooling charges, extrusion dies and various other items necessary for production of the tanks. Petitioner became the owner of the specialized equipment needed to produce its tanks (with the exception of the blow-molding machines which were used by Plastison to produce other products), and removed this equipment from Plastison's premises at the expiration of the agreement (Pet. 4; Pet. App. B, p. 6a; R. 65, 139).[1]

Plastison did not make tanks using petitioner's design unless it had an order from petitioner or anticipated such an order. Every tank made by Plastison using petitioner's design and molds was delivered to petitioner (Pet. App. B, p. 6a; R. 139, 168). Plastison neither requested nor was given permission to produce the tanks for anyone other than petitioner (R. 154). By virtue of its patent, petitioner had control over the disposition of the tanks made by Plastison (Pet. App. B, p. 6a; R. 138-139, 153-154).

Plastison paid federal manufacturers excise taxes on its sales to petitioner based on a sales price of approximately $7.50 per tank. On audit, the Commissioner of Internal Revenue determined that petitioner, rather than Plastison, was the manufacturer of the tanks for purposes of the manufacturers excise tax imposed by Section 4061(b). Accordingly, the Commissioner issued excise tax assessments against petitioner based on the retail sales

[1]"R." refers to the record appendix filed in the court of appeals.

price ($63.60) charged by petitioner to its customers.[2] The district court upheld the Commissioner's determination that petitioner was the manufacturer of the tanks. The court of appeals affirmed *per curiam* (Pet. App. A, p. 1a; Pet. App. B, pp. 2a-9a).

1. The court of appeals correctly held that petitioner was the manufacturer of the gasoline tanks in question for purposes of the excise tax imposed by Section 4061(b) on the sale of automobile accessories or parts by the manufacturer. Petitioner, of course, did not actually make the tanks. But it does not follow from this fact that petitioner was not the "manufacturer" of the tanks within the meaning of Section 4061(b). To the contrary, it has long been settled that the statutory manufacturer is the person who has the items made rather than the person who actually makes the items. See, *e.g.*, *Carbon Steel Co.* v. *Lewellyn*, 251 U.S. 501; *Polaroid Corp.* v. *United States*, 235 F. 2d 276 (C.A. 1), certiorari denied, 352 U.S. 953; *Charles Peckat Mfg. Co.* v. *Jarecki*, 196 F. 2d 849 (C.A. 7), certiorari denied, 344 U.S. 875; *Warner-Patterson Co.* v. *United States*, 68 Ct. Cl. 237; see also Treasury Regulations 46, Section 316.4(b) (1940 ed.).[3]

The courts have considered the fabricator's lack of a proprietary interest in the completed product as a critical factor indicating that the person who contracted for the

[2]The district court concluded that the proper sales price of the tanks for purposes of computing the tax imposed by Section 4061(b) was $54.50, rather than $63.60 (Pet. App. B, pp. 7a-8a). The government did not challenge that determination in the court of appeals. appeals.

[3]Treasury Regulations on Manufacturers and Retailers Excise Tax (1954 Code), Section 48.0-2(a), promulgated by T.D. 7536, 1978-18 Int. Rev. Bull. 15, which petitioner cites (Pet. 7), is not to the contrary. As subparagraph 4(ii) makes clear (Pet. App. E, pp. 22a-23a), a person who does not actually manufacture the item will nevertheless be regarded as the manufacturer under certain circumstances.

product to be fabricated, rather than the fabricator, is the statutory manufacturer. This lack of a proprietary interest arises where, as here, one company manufactures a patented item for another company which either holds the patent or is an exclusive licensee of the patent holder. Thus, if, as in this case, the person making the item for the patent holder has no right to sell or otherwise dispose of the completed item, except as directed by the patent holder, the courts have consistently held that the "first sale"[4] of the item by the manufacturer occurs not on the delivery of the item to the patent holder, but rather when the patent holder sells the item to its customers. *Charles Peckat Mfg. Co.* v. *United States, supra; Polaroid Corp.* v. *United States, supra; Warner-Patterson Co.* v. *United States, supra.* Indeed, petitioner itself recognizes (Pet. 5-6, 10) that the decisions in *Charles Peckat Mfg. Co.* and *Polaroid Corp.* squarely support the decision below.

2. Contrary to petitioner's contention (Pet. 5), *Air Lift Co.* v. *United States*, 418 F. 2d 558 (C.A. 6), affirming 286 F. Supp. 249 (W.D. Mich.), is distinguishable. In *Air Lift*, the taxpayer, which held the patent on the *use* of certain inflatable rubber cylinders as suspension devices in automobiles, contracted with another company for the fabrication of those cylinders. Unlike this case, *Peckat* and *Polaroid*, the fabricator in *Air Lift* was free to sell the rubber cylinders (which had numerous uses other than as suspension devices) to purchasers other than the taxpayer, subject only to the limitation that it not advertise their use

[4]As this Court explained in *Indian Motocycle Co.* v. *United States*, 283 U.S. 570, 574, the excise tax is not "laid on all sales, but only on first or initial sales—those by the manufacturer." Contrary to petitioner's assertion (Pet. 6), the identity of the manufacturer was not an issue in *Indian Motocycle Co.* and it consequently has no bearing on the resolution of this case.

as spring suspension devices. On the basis of this fact, the court concluded that the fabricator did have a proprietary interest in the completed product so as to make its transfer of the cylinders to the taxpayer the taxable first sale.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.,
Solicitor General.

JUNE 1978.

NO. 77-1550

IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

RECREATIONAL PRODUCTS MARKETING, INC.,
Petitioner

v.

UNITED STATES OF AMERICA,
Respondent

REPLY MEMORANDUM FOR PETITIONER

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OCTOBER TERM, 1977

RECREATIONAL PRODUCTS MARKETING, INC.,
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UNITED STATES OF AMERICA,
Respondent

REPLY MEMORANDUM FOR PETITIONER

In reply to the Government's Memorandum in Opposition, the petitioner makes the following comments:

1. We are amazed at the Government's effort (Memo., p. 4, n. 4) to avoid the conflict in principle between the decisions below and this Court's holding in *Indian Motorcycle Co. v. United States*, 283 U.S. 570, 574 (1931), that the tax applies to the first sale of the product. Even Judge (now Solicitor General) McCree recognized in his dissenting opinion in *Air Lift v. United States*, 418 F.2d 558, 559-560 (C.A. 6, 1969), that the holding in *Indian Motorcycle* raised the "more significant issue" for reso-

lution in this type of case. Little we could say would more dramatically evidence the need for plenary review to settle the rampant confusion which has lead to ad hoc and inconsistent results.

2. Ignoring *Indian Motorcycle*, the Government raises (Memo., pp. 3-4) a "proprietary interest" analysis in support of the decision below.[1] Under this analysis, a person having a "proprietary interest" in the product is the manufacturer even though he performs no act of manufacture. This would subject a patent holder to liability as a matter of law. This analysis was rejected by the courts in *Air Lift*. In an effort to avoid the conflict with *Air Lift*, the Government raises (Memo., pp. 4-5) an ad hoc refinement upon its "proprietary interest" analysis. The Government now urges that *Air Lift* is distinguishable and hence the decisions are not in conflict because in *Air Lift* the fabricator was free to sell the product to others for nonpatented and nontaxable uses. That is a factual distinction between the two cases; the presence of different facts, however, does not avoid the conflict, for the courts in *Air Lift* did not base their decisions on that distinction. Indeed, the district court there expressly rejected the Government's argument that the patent per se requires taxation of the patent holder rather than the fabricator. And, in affirming on the basis of the district court's opinion, the court of appeals summarily reviewed the pertinent

1. Although the Government states (Memo., p. 3) that the "proprietary interest" analysis is "*a* critical factor" (emphasis supplied) to resolution of the issue raised, this is the only factor now asserted by the Government in support of the decisions below. We assume that this is because other factors urged by the Government and apparently relied upon by the courts below—e.g., the discredited factor of petitioner's supplying tools—are demonstrably spurious. (See par. 5 *infra*.)

facts and neither mentioned nor hinted in any way that this distinction was pertinent to its affirmance.

3. The Government offers no support for its "proprietary interest" analysis or for the refinement it advances to distinguish *Air Lift*. The reason, of course, is that the Government cannot support either position, without rejecting this Court's holdings in *Indian Motorcycle* and in *F. W. Fitch Co. v. United States*, 323 U.S. 582 (1945). While, as noted, the Government made a spurious effort to distinguish *Indian Motorcycle*, the Government ignores altogether the blatant inconsistency between the decisions here and the holding in *Fitch*. (See Pet., pp. 12-13.) Congress did not intend in enacting this statute nor did this Court intend in deciding *Fitch* to permit the Government to have its cake and eat it too, by applying the tax to the first sales price without downward adjustment based on perceived equitable considerations but applying the tax to the second (and higher) sales price based on perceived equitable considerations. Such a startling interpretation of the statute deserves plenary review by this Court.

4. Further evidencing the need for review is the Government's inconsistent application of the "proprietary interest" analysis. The Government thus ignores its nonapplication to the name brand product, which confers an equal proprietary interest. (See Pet., pp. 11-12.) Certainly, there is nothing in the statute or in the apparent logic of the "proprietary interest" analysis which would justify the distinction. And, while this petitioner cannot avoid a tax simply because others similarly situated avoid the tax, the Government's apparent good faith exemption of the others suggests less certainty as to the merits of this analysis than the Memorandum in Opposition acknowledges.

5. Finally, the Government abandons (and correctly so, see Pet., pp. 13-14) its reliance upon the petitioner having supplied special tools and paid special charges. Yet, before both courts below the Government urged this as a consideration, and the district court below cited (Pet. App. 5a) this consideration as a significant aspect of the cases upon which it relied—*Charles Peckat Mfg. Co. v. Jarecki,* 196 F.2d 849 (C.A. 7, 1952), cert. denied, 344 U.S. 875 (1952), and *Polaroid Corp. v. United States,* 235 F.2d 276 (C.A. 1, 1956), cert. denied, 352 U.S. 953 (1956). The Government's abandonment of this spurious position casts doubt upon the authority of *Peckat* and *Polaroid,* and therefore casts doubt upon the merits of the decisions below. In any event, the Government's abandonment of this position after maintaining it for so many years further evidences significant confusion and the need for this Court to settle this area of taxation.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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